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**Single-stock ETFs a double-edged sword**
By Rob Burgess
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They're a relatively new concept, but interest in single-stock exchange-traded funds has picked up over the past two years or so.

However, experts warn that these vehicles carry inherent risks for investors.

After first appearing in Europe in 2018, the first single-stock ETFs were introduced in the U.S. in July 2022. AXS Investments became the first American company to pass a regulatory milestone to provide leveraged single-stock ETFs.

Unlike typical ETFs, they concentrate on just one security. Among the first companies featured by AXS were Tesla, Nvidia and PayPal.

There are now dozens of single-stock ETFs available.

Even when they were first approved by regulators, SEC Chair Gary Gensler and Commissioner Caroline Crenshaw voiced their concerns.

Single-stock ETFs are designed for traders who wish to speculate on the outcome of a single company's short-term price movements, said David Nash, financial planner and founder of Tend Wealth in Sherman Oaks, California. They are typically leveraged investments, meaning the goal is to magnify price changes of the particular stock that they track.

"They are a particularly risky investment, as fees, taxes and borrowing costs all add additional drags on performance," he said. "Individual stocks are already riskier than many individual investors realize, with the potential to wipe out years of gains with a single bad press release or company scandal. A single-stock ETF would only magnify that risk for investors hoping to get lucky, rather than benefit from the long-term growth of a diversified portfolio."

Jason Gilbert, founder and managing partner of RGA Investment Advisors in Great Neck, New York, said single-stock ETFs are highly speculative vehicles that often attract investors chasing short-term momentum rather than adhering to a long-term, fundamentals-driven strategy.

"These ETFs can amplify risks through leverage or by concentrating exposure to a single company, which contradicts the principles of diversification and low-turnover investing," he said. "Additionally, the frequent trading and rebalancing

required to maintain leverage or manage the ETF's exposure can lead to unintended tax consequences, including capital gains distributions. For most investors, buying the stock directly with a long-term outlook is a more tax-efficient and prudent approach. While these ETFs might appeal to those seeking quick returns or market timing, they generally don't align with disciplined investment strategies."

On the flip side, a single-stock ETF makes it easier for investors to achieve an inverse position or leverage, said Eric Papa, senior associate advisor at RS Crum in Newport Beach, California.

"The investor could take the same position without the ETF, but they would have to purchase the underlying derivatives," he said. "Buying a bear shares ETF caps the investor's loss compared to the unlimited risk that shorting a stock entails. On the other hand, they could just purchase a put option contract themselves. These ETFs aren't inherently good or bad. It lets less savvy investors take more nuanced positions."

The name single-stock ETFs can be a bit misleading, and they are usually not part of an average investor's holdings, said Melissa A. Caro, founder of the platform My Retirement Network, a digital media company.

"Investors need to be hyper-aware that they are not just buying a stock or an ETF the way they are used to," she said. "These ETFs often offer leverage or inverse exposure. Because the leverage effect resets daily, they are not ideal for long-term investments and can be quite risky."

Single-stock ETFs also can provide exposure to foreign stocks, which are not as easily available otherwise.

Arielle Tucker is the founder of Connected Financial Planning in Zurich, Switzerland, which serves American expats living and working in Europe. She said while single-stock ETFs provide an opportunity to amplify returns or hedge positions, they come with increased risk and complexity.

"These instruments can be a double-edged sword," she said. "They may be useful for experienced traders with a deep understanding of the underlying mechanics, but they are generally unsuitable for the average investor."

For the average investor, Tucker said she considers single-stock ETFs to be a risky proposition.

"The leveraged nature means that losses can be magnified just as much as gains," she said. "Additionally, these ETFs often have higher fees and can suffer from decay over time due to daily rebalancing. Therefore, unless an investor has a specific short-term strategy and fully comprehends the risks, it's usually better to steer clear."